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No. 918

In the Supreme Court of the United States

OCTOBER TERM, 1961

THE KANSAS CITY SOUTHERN RAILWAY COMPANY,
APPELLANT,

v.

JAMES S. REILY, COLLECTOR OF REVENUE, STATE OF LOUISIANA (Since Succeeded by Robert L. Roland, Who Was Duly Succeeded by Roland Cocreham),
APPELLEE.

MOTION TO DISMISS ON BEHALF OF THE COLLECTOR OF REVENUE

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Appellee, through undersigned counsel of record, respectfully moves that this appeal be dismissed on the following grounds:

No substantial federal question is raised by the facts of this case. The appointment formula set out by the Legislature of Louisiana meets all the tests of fairness and reasonableness which have been imposed on the state's power to tax by the United States Constitution as interpreted by this Court.

STATEMENT OF THE CASE

Appellant is engaged in the transportation of passengers, freight, and mail by rail in the State of Louisiana and owns all of the stock of three subsidiary corporations doing business in Louisiana. These subsidiaries and the percentage of business done by each in Louisiana during the years in controversy are as follows:

The Louisiana and Arkansas Railway Company (Delaware)

1951	73.3185%
1952	70.9843%

Kansas City Southern Transport Company (Louisiana)

1951	55.0%
1952	57.9%

Kansas City, Shreveport Gulf Terminal Company (Louisiana)

1951	100%
1952	100%

The tax involved in this litigation is the Louisiana Corporation Franchise Tax which is levied on domestic and foreign corporations doing business in Louisiana. The amount of tax paid by a corporation is determined by the amount of capital stock, surplus, and borrowed capital of the corporation and the proportion of its business which is done in Louisiana.

The extent to which the taxpayer is deemed to have used its franchise in Louisiana is determined by

the use of a two factor allocation formula based on income and assets.

ARGUMENT

The issue in this case concerns the validity of the allocation formula provided by La. R.S. 47:606. Appellant, The Kansas City Southern Railway Company, contends that paragraph B of this section as applied to it violates the due process clause of both the United States and the Louisiana Constitution.

R.S. 47:606B provides for the allocation of taxable capital within and without Louisiana as follows:

> "*Allocation of Intercompany Items.* For the purpose of allocation, investments in, advances to, or revenues from a parent or subsidiary corporation shall be allocated to Louisiana on the basis of the percentage of capital employed in Louisiana for corporation franchise tax purposes by the parent or subsidiary corporation."

This section is in effect a special provision governing the allocation of assets and revenues in the case of a parent or subsidiary corporation. Thus, if a corporation owns, in addition to its other assets within and without Louisiana, stock in a corporation which has a 50% ratio for Louisiana Corporation Franchise Tax purposes, then 50% of the investment in the subsidiary must be included in the Louisiana assets used to determine the ratio of Louisiana assets to total assets. The same must be done with revenues from a subsidiary.

This provision *does not levy a tax on the investment of Kansas City Southern in its subsidiaries* which

operate in Louisiana. It simply uses a portion of this investment and a portion of the revenues from the subsidiaries in computing two ratios which measure the extent of the capital employed by Kansas City Southern in Louisiana.

This case presents no issue of a property tax on the stock owned by Kansas City Southern. The franchise tax is an excise tax for the privilege of operating in the corporate form. The question here is the validity of the allocation formula established by the Legislature to be used in determining the proportion of a corporation's "taxable capital" to be taxed by Louisiana. This is a matter within the discretion of the Legislature.

In *New York v. Latrobe*, 279 U.S. 421, 49 S.Ct. 377, 50 S.Ct. 79, 65 ALR 1341 this Court held:

> "There is nothing in the Constitution which requires a state to adopt the best possible system of taxation. *Southwestern Oil Co. v. Texas*, 217 U.S. 114, 126, 54 L.ed. 688, 694, 30 Sup. Ct. Rep. 496; Delaware R. Tax, 18 Wall. 206, 231, 21 L. ed. 888, 896. Although permissible, a franchise tax need not be based solely on the amount of business done or property owned within the state. It may be rested on the nature of the business *(Southwestern Oil Co. v. Texas, supra; Quong Wing v. Kirkendall*, 223 U.S. 59, 56 L. ed. 350, 32 Sup. Ct. Rep. 192; *American Sugar Ref. Co. v. Louisiana*, 179 U.S. 89, 45 L. ed. 102, 21 Sup. Ct. Rep. 43; *Williams v. Fears*, 179 U.S. 270, 275, 45 L. ed. 186, 189, 21 Sup. Ct. Rep. 128. See *Connolly v. Union Sewer Pipe Co.* 184 U.S. 540, 562, 46 L. ed. 679, 690, 22 Sup. Ct. Rep. 431), or the particular

form in which it is carried on (see *Home Ins. Co. v. New York*, 134 U.S. 594, 606, 33 L. ed. 1025, 1031, 10 Sup. Ct. Rep. 593), so long as it bears some real and reasonable relation to the privilege granted or to the protection of the interests of the state (see *Robert & S. Co. v. Emmerson*, 271 U.S. 50, Supra, at p. 57 [70 L. ed. 834, 45 A.L.R. 1495, 46 Sup. Ct. Rep. 376])."

Therefore, if the statute is reasonably related to the business of Kansas City Southern and its interests in the State of Louisiana, there is no denial of due process of law.

In the case of *National Leather Co. v. Commonwealth of Massachusetts*, 277 U.S. 413, 48 S. Ct. 534 (1928) an application of a Massachusetts' excise tax was challenged. The National Leather Co. was a Maine corporation doing business in Massachusetts. It also owned the entire stock of two subsidiary corporations chartered in Maine but operating in Massachusetts. The Massachusetts tax statute levied a tax for the privilege of doing business at the rate of five dollars ($5.00) per thousand upon the value of the corporate excess employed within the commonwealth. In determining the corporate excess employed in Massachusetts the commissioner of corporations included all the capital stock of the subsidiaries operating in Massachusetts, but did not include stocks in corporations not operating in Massachusetts. The taxpayers claimed a denial of due process. In upholding the tax and the Massachusetts court this Court said:

"For present purposes it may be assumed

that the capital stocks of the two subsidiary companies had no situs in Massachusetts which brought them within the jurisdiction of that State for the purpose of imposing a direct property tax. See *Rhode Island Trust Co. v. Doughton*, 270 U.S. 69, 80, 46 S.Ct. 256 (70 L.ed. 475, 43 A.L.R. 1374). But here the statute does not impose any direct tax upon these stocks, and, as construed by the Massachusetts court, merely treats them as assets employed by the petitioner in its business within the State, and therefore requires that they be included when the total assets so employed by it are computed for the purpose of arriving at the proportionate part of the value of its own capital shares—determined by comparing the assets employed in business within the State with the total assets wheresoever employed or located —on which the excise for the privilege of carrying on its business within the State is imposed.

"It is settled law that a State may lawfully impose upon a foreign corporation a tax for the privilege of doing business within its borders which is measured by the proportionate part of its total gross receipts that are received within the State, *Maine v. Grand Trunk Ry. Co.*, 142 U.S. 217, 228, 12 S.Ct. 121, 163 (35 L.ed. 944); or by the proportionate part of its total capital stock which is represented by the property located and business transacted within the State, *Hump Hairpin Co. v. Emmerson*, 258 U.S. 290, 293, 42 S.Ct. 305 (66 L.ed. 622); *American Mfg. Co. v. St. Louis*, (C.C.A.) 8 F. (2d) 447, 450; or by the proportionate part of its total net income which is attributable to the business carried on within the State, *Underwood Typewriter Co. v. Chamberlain*,

254 U.S. 113, 120, 41 S.Ct. 45 (65 L.ed. 165); *Bass, etc., Ltd., v. Tax Comm.*, 266 U.S. 271, 282, 45 S.Ct. 82 (69 L.ed. 282).

"Here both the commissioner, the administrative officer charged with the enforcement of the statute, and the Massachusetts court, have found that the capital stocks of the two subsidiary companies were employed by the petitioner in carrying on its business within Massachusetts. We find no adequate reason for disturbing this conclusion. On the contrary, looking to the substance of the transactions and not merely to form, we think that the petitioner, through its ownership of the capital stock of the two subsidiary corporations and the control which it thereby exercised over them, did, in a very real and practical sense, employ these stocks as an instrumentality in carrying on its business within Massachusetts—to the extent, at least, that the controlled activities and property of the subsidiary corporations were within the State. *Cf Edwards v. Chile Copper Co.*, 270 U.S. 452, 456, 46 S.Ct. 345 (70 L.Ed. 678). And since the Massachusetts court did not determine whether the value of the stock in the Lawrence Company attributable to that part if its business and property in other States should have been deducted, for the reason that, as to such overvaluation, if any, a different statutory remedy was provided, we have no occasion to consider that question." (Emphasis Added)

The National Leather Company case above is on all fours with the instant case, and that case has been followed since it was decided in 1928. In that case the two subsidiaries were employed to carry on the parent

corporation's business in Massachusetts. The facts in the instant case clearly show that Kansas City Southern uses its subsidiaries in its business in Louisiana. The Kansas City Southern has 222.45 miles of mainline track in the State of Louisiana. It has approximately 750 employees in Louisiana. In addition to this very substantial business in its own name, it owns 100% of the Louisiana and Arkansas Railway Company which does about 70% of its business in Louisiana. This subsidiary is engaged in the railway business and its lines meet with those of Kansas City Southern in Shreveport and connect that city with New Orleans. The home office of the Louisiana and Arkansas is in Shreveport, and it has in Louisiana 422.74 of its total of 633.83 miles of mainline track. The Louisiana and Arkansas has no operating facilities at all in Missouri, and all of the accounting functions of this corporation are in Shreveport, Louisiana, where there is a treasurer's office.

The other two subsidiaries involved in this case are the Kansas City Southern Transport Company, a Louisiana corporation which operates a motor freight line serving the customers of the Kansas City Southern and The Louisiana and Arkansas; and the Kansas City, Shreveport Gulf Terminal Company, a Louisiana corporation which operates a depot in Shreveport, Louisiana, and does no business in any other state. All of these corporations are integral parts of the railway system known as The Kansas City Southern Lines.

Certainly the investment of Kansas City Southern in these subsidiaries represents capital employed by

Kansas City Southern. A corporation which chooses to operate through subsidiary corporations must have sound and economically desirable reasons for so doing. For the right it confers upon the corporation to exploit these advantages a state should have the right to tax.

The Legislature of Louisiana has provided a formula for allocating capital within and without Louisiana and this formula should be allowed to stand.

This Court dismissed an appeal involving the same provision being challenged here in the case of *Arkansas Fuel Oil Corporation v. Fontenot*, 225 La. 166, 72 So 2d 465, appeal dismissed 348 US 804, 75 S. Ct. 46, 99 L. Ed 635. The National Leather Co. case, supra, is on all fours and no issue which has not been decided by this Court has been raised by Appellant.

CONCLUSION

It is respectfully submitted that the allocation formula set out in La. R.S. 47:606 B is fair and reasonable and is a valid exercise of the state taxing power which does not infringe on the constitutional rights of appellant.

For the foregoing reasons it is respectfully submitted that the appeal should be dismissed.

Respectfully submitted,

S/ EMMETT E. BATSON

EMMETT E. BATSON
Counsel for Respondent

May 25, 1962

PROOF OF SERVICE

I, Emmett E. Batson, attorney of record for respondent in this matter and a member of the bar of this Court, do certify that a copy of this brief was served upon petitioner by depositing same this 25th day of May, 1962, in the United States post office, first-class postage prepaid, addressed to Honorable W. Scott Wilkinson, attorney of record for petitioner, at 17th Floor Beck Building, Shreveport, Louisiana.

S/ EMMETT E. BATSON

EMMETT E. BATSON

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